

Report of the auditor-general to the Mpumalanga Provincial Legislature and the council on the City of Mbombela Local Municipality

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the City of Mbombela Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, the financial statements present fairly, in all material respects, the financial position of the City of Mbombela Local Municipality as at 30 June 2017, and its financial performance and cash flows for the period then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

Basis for opinion

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
4. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Material uncertainty related to financial sustainability

6. I draw attention to the matter below. My opinion is not modified in respect of this matter.
7. I draw attention to note 57 to the financial statements, which indicates that the municipality incurred a net loss of R113 660 948 during the 11 months ended 30 June 2017 and, as of that date, the municipality's current liabilities exceeded its current assets by R994 774 003. As stated in note 57, these events or conditions indicate that a material uncertainty exists that may cast significant doubt on the financial sustainability of the municipality.

Emphasis of matters

8. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of opening balances

9. As disclosed in note 43 to the financial statements, the take-on balances from the former Mbombela and Umjindi local municipalities for 10 August 2017 have been restated as a result of errors in the financial statements of the former municipalities at, and for the period ended, 30 June 2017.

Material losses

10. As disclosed in note 48 to the financial statements, material losses of R73 666 512 were incurred as a result of electricity distribution losses, which represented 14,37% of the total electricity purchased.

Material impairments

11. As disclosed in note 4 to the financial statements, the trade receivables from non-exchange transactions balance was significantly impaired. The impairment of non-exchange receivables amounted to R213 591 015, which represented 77% of the total non-exchange receivables. The contribution to the provision for debt impairment was R50 749 131.
12. As disclosed in note 7 to the financial statements, the trade and other receivables from exchange transactions balance was significantly impaired. The impairment of exchange receivables amounted to R169 512 753, which represented 54% of the total receivables from exchange transactions. The contribution to the provision for debt impairment was R47 147 647.

Events after reporting date

13. As disclosed in note 58 to the financial statements, grant funding amounting to R81,1 million was not approved for rollover by the National Treasury.

Merger

14. As disclosed in note 47 to the financial statements, Mbombela Local Municipality and Umjindi Local Municipality were disestablished and a new category B municipality named City of Mbombela Local Municipality was established on 11 August 2016, as determined by the Demarcation Board in accordance with Mpumalanga Provincial Gazette No. 2687. The financial statements for the combined municipality are for the period 11 August 2016 to 30 June 2017.

Other matter

15. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosure note

16. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

Responsibilities of the accounting officer

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

18. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the intention is to either liquidate the municipality or cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

19. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

20. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

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| Report on the audit of the annual performance report |
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Introduction and scope

21. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.

22. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
23. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2017:

| Development priorities | Pages in the annual performance report |
|---|---|
| Development priority 1.1 – water supply | x – x |
| Development priority 1.2 – roads infrastructure development and storm water | x – x |
| Development priority 1.3 – electricity supply and energy management | x – x |
| Development priority 1.4 – sanitation/sewerage | x – x |
| Development priority 1.5 – waste management and greening | x – x |
| Development priority 1.7 – public transport | x – x |

24. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
25. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

Development priority 1.5 – waste management and greening

Various indicators

26. I was unable to obtain sufficient appropriate audit evidence for the reported achievements of the targets listed below. This was due to limitations placed on the scope of my work, as sufficient and appropriate evidence was not maintained throughout the year as required by the technical indicator definition. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine if the planned targets were achieved or whether any adjustments were required to the reported achievements.

| Indicator | Planned target | Reported achievement |
|--|---|---|
| Number of formalised households received basic waste collection services | 65 325 formalised households received basic waste collection services | 65 325 formalised households received basic waste collection services |
| Number of kilometres where street sweeping is provided | 50 kilometres where street sweeping is provided | 50 kilometres where street sweeping is provided |
| Number of kilometres where litter picking is provided | 250 kilometres where litter picking is provided | 250 kilometres where litter picking is provided |

27. I did not raise any material findings on the usefulness and reliability of the reported performance information for the following development priorities:

- Development priority 1.1 – water supply
- Development priority 1.2 – roads infrastructure development and storm water
- Development priority 1.3 – electricity supply and energy management
- Development priority 1.4 – sanitation/sewerage
- Development priority 1.7 – public transport

Other matters

28. I draw attention to the matters below.

Achievement of planned targets

29. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year and explanations provided for the underachievement of a significant number of targets. This information should be considered in the context of the material findings on the reliability of the reported performance information in paragraph 25 of this report.

Adjustment of material misstatements

30. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of water supply, electricity supply and energy management, and waste management and greening. As management subsequently corrected only some of the misstatements, I raised material findings on the reliability of the reported performance information.

Report on the audit of compliance with legislation

Introduction and scope

31. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

32. The material findings in respect of the compliance criteria for the applicable subject matters are as follows:

Expenditure management

33. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.

Procurement and contract management

34. Quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by supply chain management (SCM) regulation 13(c).

35. Awards were made to providers who were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44.

36. Some commodities designated for local content and production were procured from suppliers who did not meet the prescribed minimum threshold for local production and content, as required by preferential procurement regulation 9(5).

Other information

37. The municipality's accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report thereon and those selected development priorities presented in the annual performance report that have been specifically reported on in the auditor's report.

38. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.

39. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work I have performed on the other information obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact.

40. I have read the other information included in the draft annual report and have nothing to report in this regard.

41. I have not yet received the final annual report containing the other information. When I do receive this information, and if I conclude that it contains a material misstatement, I am required to communicate the matter to those charged with governance and to request the other information to be corrected. If the other information is not corrected, I may have to re-issue my auditor's report amended as appropriate.

Internal control deficiencies

42. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with legislation included in this report.

Financial and performance management

43. The recording, reviewing and reporting process and controls over the actual achievements of planned targets reported in the annual performance report were not adequate.

44. Non-compliance with legislation could have been prevented had compliance been properly reviewed and monitored.

Auditor-General

Mbombela

30 November 2017



**AUDITOR-GENERAL
SOUTH AFRICA**

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in the auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control.
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor's report. However, future events or conditions may cause the municipality to cease to continue as a going concern.
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.